

**BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE**

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IN RE: NOTICE OF RULE-MAKING-RULE
1220-4-2.-59 ("Special Contracts")
REGULATIONS FOR THE PROVISIONING
OF TARIFF TERM PLANS AND SPECIAL
CONTRACTS.

DOCKET NO. 00-00702

EXECUTIVE SECRETARY

**COMMENTS OF THE ATTORNEY GENERAL AND
REPORTER, PAUL G. SUMMERS, THROUGH THE
CONSUMER ADVOCATE AND PROTECTION DIVISION**

Paul G. Summers, Attorney General and Reporter, through the Consumer Advocate and Protection Division of the Office of the Attorney General and Reporter for the State of Tennessee ("Attorney General"), respectfully submits the following comments in response to the Tennessee Regulatory Authority's Notice of Rulemaking — Rule 1220-4-2.-59 ("Special Contracts") Regulations for the Provisioning of Tariff Term Plans and Special Contracts (hereinafter "Special Contracts Rules"). The comments are submitted in the Attorney General's public interest role of protecting consumers through his enforcement and investigatory power under the Consumer Advocate and Protection Division's activities before the Tennessee Regulatory Authority ("Authority").

POSTED
11-14-20

OVERVIEW

By way of overview, the Attorney General contends that special contracts with high charges for ending or terminating a multi-year contract for telecommunications services have a strong anti-competitive impact on customers because it inhibits the customers' ability to make buying choices based on price and service. As a result, the Attorney General advocates that any such termination or ending fees be as small as possible to foster and encourage competition in the State of Tennessee. Further, the Attorney General specifically requests that termination charges be small to permit consumers to take advantage of the better service and savings that competition brings about over time.

The Attorney General supports the efforts of the Tennessee Regulatory Authority ("Authority") to introduce competition into this market. While the policy decisions of the Authority necessarily require it to make choices as to timing and degree of changes, the new rule is certainly a good step in the correct direction toward allowing the businesses involved to compete equally for the privilege to provide a good service at a good price to the target customers.

While the focus of the rule is the termination penalties involved, the Attorney General encourages the Authority to adopt the filing requirements of the proposed rule as well. The filing requirements are vital to assisting the Authority and its staff in limiting the possible circumvention of the substance of the rule and the policy it seeks to encourage. Further, the Attorney General encourages the Authority to apply the new rule retroactively, thus fostering a climate of competition now rather than 4 or 5 years from now.

GENERAL DISCUSSION

The Attorney General prefers that any termination charges be reasonably related to the telecommunications company's actual cost associated with terminating the contract. Under the present environment, these termination charges are penal in nature and bear little relation to the telecommunications actual cost. Termination charges in a tariff plan or special contract are derived from the difference between services priced at a tariff rate and the services priced at a discount rate over the entire duration of the contract. For example, services priced according to the tariff may create revenue of \$500,000 for the telecommunications carrier but it may offer a discount to the customer where revenues are \$400,000. If the customer enters the contract but wishes to terminate it halfway through after having provided only \$200,000 to the carrier, then the termination charges would be \$300,000. Said another way, the lower the discount revenues, the higher the customer's termination charges.

This gives the provider a powerful economic incentive to drive down its discounted price to the minimum sustainable under Tenn. Code Ann. § 65-5-208(c), which provides that a company must adhere to a price floor. There is little risk for the provider, who stands to be "made whole" by termination charges since their foundation is laid on the gross (tariff) revenues of \$500,000 rather than the net(discount) revenues of 400,000. This process subverts a customer's normal economic behavior when comparing alternative providers of a given service because the comparison includes not just the price of the service and its quality, but also disproportionately large termination charges.

Furthermore, since the telecommunications providers are operating under price-cap regulation, the tariffs do not require cost justification. Thus the companies have the freedom to

set the tariffs at any price level they choose, provided the company complies with an overall revenue constraint. Therefore, tariffs may be well above that required of a company to offer the service. That providers offer a discount begs the question why the tariff is set as high as it is in the first place, suggesting that tariff levels may be set with an intent to create high termination charges which hinder customer choice.

The customer's cost of switching to another provider, who may well have superior technology, is driven up, delaying the day when more efficient technology penetrates the market. Termination charges truly have an anti-competitive effect and work against the Tennessee General Assembly's declaration of a telecommunications service policy whereby "the policy of this state is to foster the development of an efficient, technologically advanced statewide system of telecommunications services..." Tenn. Code Ann. § 65-4-123. Customers change carriers not only to receive lower rates but to obtain more advanced services as well. Excessive termination charges, therefore, impede the spread of more technologically advanced services.

The proposed rule is certainly a good step toward providing a solution to this problem. The Attorney General strongly supports the Authority's efforts.

Any suggestions that the filing requirements would be burdensome appear belied by BellSouth's experiences, as described at the October 18, 2000 hearing.

The lone change the Attorney General asks the Authority to consider is making the new rule apply retroactively rather than prospectively. Open competition in this area is well overdue. A "special contract" supposedly represents the free choices of buyers and sellers and assumes the premise that neither party induces the other to accept terms harmful to their respective self

interest. But it has long been recognized that individually beneficial decisions can have harmful cumulative effects.

The links between individual decisions and their overall effect was examined in "The Tyranny of Small Decisions," an essay written in 1966 by Alfred E. Kahn, who wrote:

A market economy makes its major allocations decisions on the basis of a host of 'smaller decisions . . . [But] the consumer can be victimized by the narrowness of the context in which he exercises his sovereignty . . . [I]f enough people vote for X, each time necessarily on the assumption that Y will continue, Y may, in fact, disappear . . . , a genuine deprivation that customers might willingly have paid something to avoid.

In the context of rulemaking, Y is the new competitor with the more efficient technology who seeks to compete with X on terms of price and quality instead of termination fees. But if termination fees constantly tilt individual decisions to X, Y will never reach consumers, the more efficient technology will not be used and the entire economy is worse off. The Attorney General urges the TRA to take the long, broad view recognizing that individual decisions are being unduly influenced by termination fees and that such influence must be greatly reduced for competitive telecommunications markets to flourish in Tennessee.

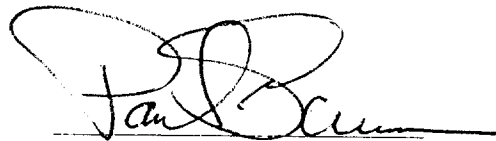
The Attorney General concurs with comments of counsel for NEXTLINK, made at the hearing of October 18, 2000 that special contracts are tariffs and subject to change at the Authority's order, just like any other tariff is subject to the Authority. These remarks provide a real life example of the constraints on trade presently prevalent. Therefore, the new rules should be applied to all tariff plans and special contracts, not just those entered into after the rules are adopted.

The Attorney General supports the Authority's interest in leveling the playing field in this market. The proposed rules, if applied to all parties and all contracts, are a significant step toward balancing the interests of business and consumer.

CONCLUSION

Consistent with its comments, the Attorney General recommends the new rule to the Authority. If the Authority needs any additional information or clarification of these Comments, please contact Timothy C. Phillips, Assistant Attorney General.

RESPECTFULLY SUBMITTED,



PAUL G. SUMMERS

Attorney General & Reporter

B.P.R. No. 6285



TIMOTHY C. PHILLIPS

Assistant Attorney General

B.P.R. No. 12751

Consumer Advocate and Protection Division

425 Fifth Avenue North

Nashville, Tennessee 37243

(615) 741-3533